

# INSURANCE COUNSELOR

## Insurance Consumer Information Sheet

### Frequently Asked Questions About Insurance Credit Scoring

In Michigan, most insurance companies **cannot** use insurance credit scoring to refuse to write an automobile or home insurance policy, cancel a policy or non-renew a policy based on a person's insurance credit score. However, many insurance companies have started to use insurance credit scoring in determining the premium a person will pay. For policies written on an individual basis, this is applied as a discount that a person may or may not be eligible for depending on the person's insurance credit score.

The Office of Financial and Insurance Services (OFIS) has assembled some of the most common questions consumers ask when learning about insurance credit scoring and have developed some answers to help clarify this complex issue. If you find after reading this information that you still have some questions, please call us toll-free at 877-999-6442.

#### **How are insurance rates set?**

In Michigan, how insurance rates can be set is outlined by law. It is an important distinction to say "outlined" because the governor, legislature and insurance commissioner cannot set insurance rates. Rather, insurance companies set rates by following permitted practices as outlined in the insurance code and rates are subject to market influences. The market influences are also important; if an insurance company sets a rate that is higher than competitors' rates, then that insurance company will have a difficult time keeping customers. This is one

reason why consumers should always shop around for insurance.

#### **What is an insurance rate discount?**

As part of the law regarding insurance rates, Michigan insurance companies can offer discounts on rates. In essence, an insurance company sets a base rate and files a list of discounts that can be offered. Since insurance companies cannot use surcharges (except with insurance sold on a group basis), the rate cannot increase from the base rate. However, base rates can, and do, experience inflationary increases.

Discounts can be extremely varied and some are directly related to types of insurance. For instance, automobile insurance rates can be discounted if a driver's car has antilock brakes, if the driver wears a seat belt or if the driver has a clean driving record. These discounts intuitively make sense; having antilock brakes can help prevent an auto accident, decreasing the chance of an auto insurance claim and making auto insurance less expensive. These savings should be factored into consumers' insurance rates.

#### **What does Michigan law say about insurance rate discounts?**

The law does not limit the type, number or content of insurance discounts. However, discounts must reflect expected reductions in losses. In addition to the discounts listed above, Michigan consumers can qualify for a good student discount or receive a discount for staying with the same insurance company.

A discounted insurance rate is great news for consumers. However, some discounts are not intuitive. Are “A” students really better drivers? Is it less expensive if a consumer stays with an insurance company for five years? The answer to both of these questions is yes and Michigan law allows an insurance company to discount insurance rates in both instances.

The use of credit information to set insurance rates falls into the category of discounts that do not intuitively make sense. The OFIS credit scoring report summarizes studies about insurance company credit scoring. The studies show that there is a link between credit history and the likelihood of making an insurance claim; consumers with poor credit histories are more likely to file an insurance claim. The report also found that credit scoring is a legal practice under Michigan law.

**When will my insurance company have to provide me with more information on credit scoring?**

Starting with July 2003 renewals, the commissioner has directed insurance companies to give Michigan consumers more information. At least once annually at renewal, an insurer is required to tell the policyholder what his or her credit score is and in which discount tier he or she has been placed.

**Can an insurance company look at my credit information without my permission?**

Yes. The Fair Credit Reporting Act (FCRA) says that insurance companies may look at your credit information without your permission for underwriting practices.

**How long have insurers used credit information to set insurance rates?**

Credit scoring is a relatively new practice and started in Michigan in the late 1990’s.

**Are people with poor credit histories more likely to make an insurance claim?**

Some studies have shown that there is a link between credit history and the likelihood of making an insurance claim. Insurance regulators and actuarial associations continue to study this issue, especially because the studies have not discovered why this link exists. The OFIS credit scoring report contains legislative recommendations and notes that the Michigan Legislature may wish to fund a comprehensive study of outstanding issues pertaining to credit scoring.

**If I have really good credit, am I sure to get a better rate on my insurance?**

If you have really good credit and your insurance company uses credit scoring, you will get a discount. Each insurance company that uses credit scoring can set different formulas to establish credit scores and different levels of discounts for each score, so the amount of discount available will differ among insurance companies.

**Can OFIS help consumers identify insurers who use credit information to discount rates?**

Yes. OFIS has a list of insurance companies that use credit scoring in the credit scoring section of its Web page, and the information can be directly linked at [www.michigan.gov/documents/cis\\_ofis\\_credentials\\_lst\\_26800\\_7.pdf](http://www.michigan.gov/documents/cis_ofis_credentials_lst_26800_7.pdf). The OFIS credit scoring report has additional insurance company credit scoring information and can be directly linked at [www.michigan.gov/documents/cis\\_ofis\\_credit\\_scoring\\_report\\_52885\\_7.pdf](http://www.michigan.gov/documents/cis_ofis_credit_scoring_report_52885_7.pdf). The list and report are also available by calling OFIS toll-free at 877-999-6442.

### **How can I find an insurer who will give me a better rate based on my credit history?**

Insurers set premiums using many factors. A consumer can find the lowest overall premium by shopping around generally.

### **What kind of credit information do insurance companies use?**

Most companies that use credit information use an "insurance credit score." An insurance credit score is calculated using information about your credit history. Many insurance credit scores are weighted using recent credit history more heavily than old credit history. The factors used in many scoring models are:

- **Public records** (such as bankruptcy, collections, foreclosures, liens, and charge-offs). Public records generally have a negative effect on your insurance credit score.
- **Past payment history** (the number and frequency of late payments and the days between due date and late payment date). Late payments tend to have a negative effect on your insurance credit score.
- **Length of credit history** (the amount of time you've been in the credit system). A longer credit history tends to improve your insurance credit score.
- **Inquiries for credit** (the number of times you've recently applied for new credit, including mortgage loans, utility accounts, and credit card accounts). Shopping for new credit tends to have a negative effect on your insurance credit score.
- **Number of open lines of credit** (including the number of major credit cards, department store credit cards). Having too much credit tends to have a negative effect on your insurance credit score. However, it generally is not a good idea to cancel a credit account that you have had for a long time. A long credit history may help your score.

- **Type of credit in use** (such as major credit cards, store credit cards, finance company loans, etc). Major credit cards may be treated more favorably than other types of consumer credit, such as store credit cards or loans from a finance company.
- **Outstanding debt** (how much you owe compared to your available credit). Too much outstanding debt tends to have a negative effect on your insurance credit score.

### **Can I ask to have my insurance credit score recalculated if my credit has improved to obtain a discount or a larger discount?**

Yes. On May 14, 2003 the commissioner issued a Bulletin about re-scoring. At the request of the policyholder, a company must re-score at least once annually. Consumers should consider the factors above to determine if their credit history has improved in the last year. If not, re-scoring might cause the policyholder to get a higher premium. There are some things consumers would think would improve a credit history but might end up lowering their credit score, and thus increasing their premium, such as refinancing a home, opening a home equity line of credit, and changing to a lower interest rate credit card.

### **If I don't know my score, and my score varies from company to company, how will I know if my credit history affects my insurance purchases?**

Ask your insurance agent or company. The FCRA requires an insurance company to tell you if they take an "adverse action" because of your credit information. FCRA defines "adverse action" to include denying or canceling coverage, increasing premiums, or changing the terms, coverage, or amount of coverage in a way that harms the consumer. Examples of "adverse action" include:

- Canceling, denying or non-renewing coverage.
- Giving the consumer a limited coverage form.
- Limiting benefits, such as eligibility for dividends.
- Issuing coverage other than that applied for.
- Not giving the consumer the best rate.
- Not giving the consumer the best discount.
- Adding a premium surcharge.

If your insurer takes an adverse action due to your credit history, it must also tell you the name of the national credit bureau that supplied the information. You are also entitled to a free copy of your credit report from the credit bureau that supplied the credit information.

Federal law says you have a right to a free copy of your credit report if you have been denied credit or insurance, if you are on welfare, unemployed, or if you are a victim of identity theft. Otherwise, you may have to pay a small fee for the report. Most consumer groups suggest you get a copy of your credit report once a year and review it for errors.

### **I have a problem with my insurance and I want some help. What can I do?**

If a consumer cannot resolve an insurance problem by contacting the insurance company and agent, OFIS is available for assistance. Consumers should contact OFIS toll-free at 877-999-6442 to speak with consumer assistance staff. A complaint form can be mailed or faxed and is available directly at [www.michigan.gov/documents/cis\\_ofis\\_complaint\\_all\\_25074\\_7.pdf](http://www.michigan.gov/documents/cis_ofis_complaint_all_25074_7.pdf).